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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

In the Matter of

Access Charge Reform

Price Cap Performance Review
for Local Exchange Carriers

DOCKET FILE COPY ORIGINAL

CC Docket No. 96-262

CC Docket No. 94-1

REPLY TO OPPOSITIONS
TO PETITION FOR RECONSIDERATION

The Association for Local Telecommunications Services ("ALTS") and Focal Communications Corporation ("Focal") (collectively "Petitioners") submit this Reply to the Oppositions filed by the Coalition for Affordable Local and Long Distance Services ("CALLS") and Sprint Corporation ("Sprint") to ALTS' and Focal's Petition For Reconsideration of the *CALLS Order*.

I. INTRODUCTION

In its Opposition, Sprint verifies that the Commission in adopting the CALLS plan has abandoned price cap regulation. It informs us that "the access reform plan adopted in the *CALLS Order* is not an incremental change in price cap regulation; instead, it is a sea change in the way the Commission regulates LEC access charges."³ Similarly, it refers to price cap regulation in the past tense.⁴ Indeed, the *CALLS Order* does establish a fundamental change in the regulation of price

³ Sprint Opposition, p. 2.

⁴ *Id.* (referring to application of the X-Factor based on productivity "as was the case with price cap regulation")

cap ILEC interstate access charges by setting rates based on partial industry negotiations instead of the price cap formula.

The heart of the Commission's justification for this radical departure from the price cap formula as the mechanism for regulating price cap ILEC interstate access charges, and adoption of the CALLS plan in general, including X-Factor targeting, is that it represents a negotiated solution to access reform issues. The Commission viewed the CALLS plan as an "industry consensus plan" for achieving access reform.⁵ Similarly, the Commission viewed X-Factor targeting as a "compromise" to contentious X-Factor prescription proceedings. However, there was no industry consensus for adoption of the CALLS plan. While a consensus may have been the goal of CALLS deliberations, it was not achieved. CLECs did not support the CALLS proposal. Nor did all ILECs or IXC's. MCI WorldCom and USWest (now Qwest) dropped out of the CALLS coalition. Qwest actively opposed the CALLS plan before the Commission. Moreover, the only way the Commission could get all price cap ILECs on board with the CALLS plan was to threaten them with setting rates based on cost studies if they don't go along. Nor was there any compromise concerning application of the X-Factor, except among CALLS members. And, the CALLS plan is completely inconsistent with the price cap formula. CALLS members and the Commission have treated the various components of the price cap formula, including the X-Factor, as so many tinker toys that may be combined in any which way as long as those involved in negotiation of the CALLS plan agree.

Furthermore, the CALLS plan was legally dead on arrival because the Commission has not established, or invoked, any procedural framework, standards, or rules for achieving a negotiated

⁵ *CALLS Order*, para. 35.

solution to access reform or setting interstate access rates through negotiation instead of the price cap formula. Accordingly, the negotiated price cap rules and negotiated rates adopted by the Commission in the *CALLS Order* are completely arbitrary in substance and in the process that was followed to adopt them. The Commission should promptly grant reconsideration and reset rates in accordance with previous price cap rules. The Commission should also direct CALLS to terminate any further consumer education efforts since there is no point in educating consumers about unlawful rule changes and because these efforts will only make it more difficult to reset rates on a lawful basis.

II. THE COMMISSION DID NOT PROVIDE A REASONED EXPLANATION OF X-FACTOR TARGETING

A. CALLS and the *CALLS Order* Provide No Explanation For ILEC Discretion to Apply X Factor Reductions to Any Average Traffic Sensitive Rate Elements

Contrary to CALLS contentions, the Commission did not provide a “reasoned explanation” for X-Factor targeting under the CALLS Plan.”⁶ Among other arbitrary aspects of the plan, ILECs’ discretion under the plan to apply X-Factor reductions in any way they choose to different rate elements in traffic sensitive baskets as long as the average target price is achieved remains completely unexplained.⁷ Petitioners pointed out prior to the adoption of the *CALLS Order* that this aspect of the plan would grant premature pricing flexibility.⁸ The *CALLS Order* did not address this concern. In its present Opposition, CALLS merely admits that its plan grants price cap ILECs

⁶ CALLS Opposition, p. 4.

⁷ “Carriers, however, may take these reductions against any of the average traffic sensitive charge rate elements, provided that they still generate the same amount of reductions.” CALLS Memorandum, p. 12.

⁸ Focal Comments, pp. 5,10.

“freedom to choose where to target reductions in the price caps.”⁹ CALLS provides absolutely no explanation as to why price cap ILECs should have the flexibility to apply X-Factor reductions anywhere among switched access rate elements. In fact, this is a blatant misuse of the X-Factor that will permit ILECs to use the X-Factor to fund rate reductions in response to competition or for whatever purpose ILECs choose. Obviously, this grants ILECs premature pricing flexibility for switched services. Again, this is another negotiated aspect of the CALLS plan that makes no sense whatsoever. The Commission’s adoption of it without explanation was arbitrary and unlawful in the truest sense in that there is no explanation for this aspect of the plan either in the plan itself, the *CALLS Order*, or the present CALLS’ Opposition.

B. Targeting Is Not Justified On this Record on the Basis of Costs

In its Opposition, Sprint contends that X-Factor targeting to switching is justified because technological changes have reduced the costs of the switching component of access more than other components of access.¹⁰ It states that it has placed on the record substantial evidence in the record to this effect on which the Commission relied in the *CALLS Order* and that this justifies the targeting of the X-Factor to switching.¹¹

Petitioners submit that there is an insufficient basis in the present record for setting switching rates based on costs. If there were a sufficient record basis for setting rates based on costs, the Commission would not have found it necessary to require ILECs not opting into the CALLS plan to submit cost studies.

⁹ CALLS Opposition, p. 7.

¹⁰ Sprint Opposition, pp. 3-4.

¹¹ Sprint Opposition, p. 4, citing *CALLS Order*, n. 376.

Moreover, the price cap formula sets rates based on a regulation of price. The price cap formula does not set rates based on carriers' costs.¹² The casual reference to costs in a footnote in the *CALLS Order* is an insufficient basis to set switched access rates based on costs or to convert price cap regulation to cost-based regulation. Nor was there any explanation in the *CALLS Order* as to how the reference to a smattering of incomplete cost and rate-of-return data could be used to set uniform switching rates among broad categories of price cap ILECs who presumably have at least somewhat different costs.

In addition, cost does not justify X-Factor targeting to switching when price cap ILECs have so much discretion as to which switching elements the targeting will apply. Given that ILECs can apply targeting to any switched rate elements as long as the average traffic sensitive target rate is achieved -- regardless of costs -- there is no basis for a conclusion that switching rates achieved through CALLS plan X-Factor targeting are based on costs.

C. ALTS Counter Proposal Does Not Justify the Calls Plan

CALLS and Sprint contend that the arbitrary X-Factor targeting and target switching rates of the CALLS plan are acceptable because ALTS, as an alternative to the CALLS plan, proposed a plan which also involved targeting, but that would achieve target rates over a more extended timeframe.¹³ Petitioners have contended throughout this proceeding that the targeting of X-Factor reductions to switching is arbitrary and unlawful. ALTS chose to develop an alternative plan that borrowed heavily from the CALLS plan in the hope that the Commission would adopt a plan less

¹² *Policy and Rules Concerning Rates for Dominant Carriers*, CC Docket No. 87-313, 5 FCC Rcd 6786 (1990) ("*LEC Price Cap Order*"); *Price Cap Performance Review for Local Exchange Carriers*, CC Docket No. 94-1, 10 FCC Rcd 8961, 9027 ("*Price Cap Performance Review Order*").

¹³ CALLS Opposition, p. 4.

damaging to CLECs. Petitioners have never endorsed any X-Factor targeting as reasonable or lawful simply because some industry participants have proposed it. It is possible that targeting could be lawful based on a true industry consensus including CLECs adopted pursuant to appropriate negotiation procedures. Accordingly, CALLS must find some other basis for justifying its proposal rather than ALTS' pragmatic proposal for a more reasonable outcome to this proceeding in the context of the Commission's rush to adopt the CALLS plan.

III. THE COMMISSION MAY NOT ON THIS RECORD SET RATES BASED ON NEGOTIATION

While it might be possible for the Commission to establish a scheme under which price capped rates could be set on the basis of negotiation among industry participants, rather than the price cap formula, the Commission has not established any such scheme. The Commission has not established any rules, standards, or procedures, either of general applicability or for application in this specific instance, that could provide a basis for setting price capped rates or adopting rule changes based on industry negotiations. For example, the Commission has not adopted any procedures generally, nor did it establish any in this instance, to assure that all interested parties participated in such negotiations seeking to develop an industry consensus plan. Accordingly, the Commission's adoption of the CALLS proposal as reasonable negotiated rates and rule changes was inherently arbitrary, apart from the fact that there was no industry consensus in any event.

At least some CALLS members reportedly view Commission deliberations leading up to adoption of the *CALLS Order* as a negotiated rulemaking.¹⁴ Petitioners agree with CALLS that the Negotiated Rulemaking Act is an optional process by which the Commission can seek to obtain an

¹⁴ Communications Daily, September 27, 2000, p. 2 (quoting a BellSouth official as describing the CALLS process as a "negotiated rulemaking.")

industry consensus proposal as part of a rulemaking. However, since the Commission chose not to invoke those optional processes there is no basis for concluding that the Commission has conducted a negotiated rulemaking pursuant to that section. To the extent that the Commission has authority to conduct negotiated rulemaking apart from the Negotiated Rulemaking Act, the Commission has not, as stated, established any rules or procedures governing such a process. For that reason, the Commission's reliance on negotiations as the basis in this instance for adjusting capped rates, rather than the price cap formula, was unlawful. Accordingly, the Commission must promptly grant reconsideration and reset rates in accordance with the price cap formula.

IV. ANY CHANGES TO PRICE CAP REGULATION BASED ON NEGOTIATION MUST REFLECT CLEC VIEWS

CALLS suggests that Petitioners in this proceeding are seeking merely to preserve a "major source of CLEC revenues."¹⁵ Petitioners object in the strongest possible terms to the supposition that CLECs' interests in this proceeding are somehow not entitled to serious consideration because they are centered around the fact that CLECs are competitors to ILECs in provision of interstate access services and will be seriously affected by changes in regulation of ILEC interstate access charges. CALLS statement surely constitutes disingenuousness to the highest degree given that preservation of interstate access revenues and reductions of same are ever burning fiercely in the constellation of regulatory goals of ILECs and IXCs, respectively. Indeed, CALLS members have handsomely served their self-interest in the CALLS plan in that "access reform" in this instance has

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CALLS Opposition p. 3, quoting ALTS/Time Warner Comments at 10.

been accomplished while preserving ILEC revenues and reducing charges to IXCs, in part by shifting recovery to end users ¹⁶ and a new arbitrary universal service fund.

Moreover, under the CALLS plane ILECs are able to misuse the X-Factor to fund reductions in switching and obtain a “glidepath” to a soft-landing to lower switching rates. On the other hand, ALTS’ proposal in this proceeding to establish a moderated “glidepath” in light of the significant impact that the proposed sudden reductions could have on CLECs was somehow not a valid issue that the Commission needed to assure was reflected in an industry negotiated access reform plan. A “glidepath” to reduced switching rates is precisely the type of issue that would have been appropriate for industry negotiations, including CLECs, given the adverse impact on CLECs. Insofar as the Commission is going to be so solicitous of ILEC needs so as to assure that they will have a soft landing to reduced switched access charges - even by means of arbitrary and unlawful X-Factor rule changes - the Commission should be equally sensitive to CLEC needs in this area especially at a time when CLECs as new competitors are experiencing heightened market difficulties.¹⁷ The CALLS plan provides an ample soft-landing to ILECs, but none to CLECs, which is not surprising given the incomplete industry participation in CALLS negotiations. The Commission has previously recognized that access reform must be carefully crafted to enhance competition. Accordingly, the Commission must on reconsideration include CLECs in any future negotiated solutions to access reform, assuming that the Commission pursues further industry negotiated plans as a way of achieving access reform. Petitioners submit that the exclusion of

¹⁶ Under the CALLS plan, switched access reductions will not “generally” be subsidized by increasing non-traffic sensitive flat-rated end-user fees. *CALLS Order*, paras. 152.

¹⁷ See, e.g. Small Phone Companies Losing Ground to Telecom Giants, CnetNews.com, <http://news.cnet.com/news/0-1004-201-2932468-0.html?tag=st.ne.1004.ttext.sf>, October 6, 2000.

CLECs from the CALLS “industry consensus plan” renders the Commission’s adoption of it unlawful.

V. THE UNIVERSAL SERVICE FUND REMAINS UNJUSTIFIED

As stated previously by Petitioners, the Commission had no factual or cost basis for choosing \$650 million as the size of the new universal service fund.¹⁸ As with the rest of the CALLS plan, the only basis for this is that it was a negotiated result. Thus, the Commission stated that “the negotiated nature of the \$650 million estimate provides strong evidence that \$650 million will be sufficient ...”¹⁹ Relying on negotiation for determining the size of this universal service fund is unlawful for all the reasons stated previously.

CALLS also repeats that AT&T, using a cost model, produced estimates consistent with \$650 million.²⁰ However, this provides absolutely no support for \$650 million because all other CALLS members refuse to endorse use of cost models for determining universal service support and have made it clear they reserve the right to walk away from this figure.²¹

CALLS also contends that ALTS and Focal lack credibility on this issue because “ALTS and Focal have themselves advocated a \$300 million fund that lacks any empirical support or explanation.”²² Petitioners view this statement as at least implicit agreement that the \$650 million selected by the Commission lacks any empirical support or explanation. More importantly, as stated

¹⁸ Petition for Reconsideration, pp. 14-16.

¹⁹ *CALLS Order*, para. 202.

²⁰ *CALLS Opposition*, n. 5.

²¹ *Id.*

²² *CALLS Opposition*, p. 7.

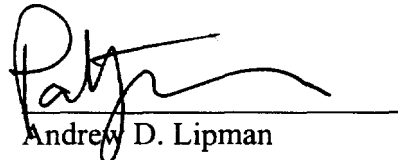
above, the ALTS alternative plan borrowed liberally from the CALLS plan in the hope that this might produce a result less unfortunate for CLECs. Petitioners would prefer that the Commission determine universal service funds on the basis of cost models. Petitioners do not believe that the \$650 million fund established by the Commission is anything other than completely arbitrary and drawn from little more than thin air.

VI. CONCLUSION

Accordingly, the Commission should rescind its approval of the CALLS plan, and direct price cap ILECs to reestablish rates set in accordance with price cap rules prior to adoption of the *CALLS Order*.

Jonathan Askin, General Counsel
Teresa K. Gaugler
Association for Local Telecommunications
Services
888 17th Street, N.W., Suite 900
Washington, D.C. 20006
(202) 969-2587

Respectfully submitted,



Andrew D. Lipman
Patrick J. Donovan
Swidler Berlin Shereff Friedman, LLP
3000 K Street, N.W., Suite 300
Washington, DC 20007
(202) 424-7500

Counsel for Focal Communications
Corporation

Richard Metzger
Vice President
Regulatory Affairs and Public Policy
Pamela Arluk
Focal Communications Corporation
7799 Leesburg Pike - Suite 850 N
Falls Church, VA 22043
(703) 637-8778

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CERTIFICATE OF SERVICE

I, Candise M. Pharr do hereby certify that on this 11th day of October, 2000 the foregoing Reply to Oppositions Petition to Petition for Reconsideration of Focal Communications Corporation were delivered by hand and first class mail to the following:


Candise M. Pharr

VIA HAND DELIVERY

Debra Weiner
Federal Communications Commission
445 12th Street, S.W. - The Portals
Washington, DC 20554

Rebecca Beynon
Federal Communications Commission
445 12th Street, S.W. - The Portals
Washington, DC 20554

VIA HAND DELIVERY

Kyle D. Dixon
Federal Communications Commission
445 12th Street, S.W.
The Portals
Washington, DC 20554

VIA HAND DELIVERY

Christopher Wright
Federal Communications Commission
The Portals - 445 12th Street, S.W.
Fifth Floor
Washington, DC 20554

VIA HAND DELIVERY

Dorothy Atwood
Federal Communications Commission
Common Carrier Bureau
445 12th Street, S.W. - Suite 5A848
The Portals
Washington, DC 20554

VIA HAND DELIVERY

Jane E. Jackson
Federal Communications Commission
The Portals
445 12th Street, S.W.
Washington, DC 20554

VIA HAND DELIVERY

Richard Lerner
Federal Communications Commission
The Portals
445 12th Street, S.W.
Washington, DC 20554

VIA HAND DELIVERY

Tamara Preiss
Federal Communications Commission
The Portals
445 12th Street, S.W.
Washington, DC 20554

VIA HAND DELIVERY

Chairman William E. Kennard
Federal Communications Commission
445 12th Street, S.W. - Suite B201
The Portals
Washington, DC 20554

VIA HAND DELIVERY

Laurence Bourne
Federal Communications Commission
445 12th Street, S.W.
The Portals
Washington, DC 20554

VIA HAND DELIVERY

Aaron Goldschmidt
Federal Communications Commission
445 12th Street, S.W.
The Portals
Washington, DC 20554

VIA HAND DELIVERY

Anna Gomez
Office of Chairman William E. Kennard
Federal Communications Commission
445 Twelfth Street, S.W.
Washington, DC 20554

VIA HAND DELIVERY

Commissioner Susan Ness
Federal Communications Commission
445 Twelfth Street, S.W.
Washington, DC 20554

VIA HAND DELIVERY

Jordan Goldstein
Office of Commissioner Susan Ness
Federal Communications Commission
445 Twelfth Street, S.W.
Washington, DC 20554

VIA HAND DELIVERY

Commissioner Harold Furchtgott-Roth
Federal Communications Commission
445 Twelfth Street, S.W.
Washington, DC 20554

VIA HAND DELIVERY

Commissioner Michael K. Powell
Federal Communications Commission
445 Twelfth Street, S.W.
Washington, DC 20554

VIA HAND DELIVERY

Commissioner Gloria Tristani
Federal Communications Commission
445 Twelfth Street, S.W.
Washington, DC 20554

VIA HAND DELIVERY

Deena Shetler
Office of Commissioner Gloria Tristani
Federal Communications Commission
445 Twelfth Street, S.W.
Washington, DC 20554

John T. Nakahata
Samuel L. Feder
Harris, Wiltshire & Grannis LLP
1200 Eighteenth Street, NW
Washington, DC 20036

Mark C. Rosenblum
Judy Sello
AT&T Corp
295 North Maple Avenue – Room 1135L2
Basking Ridge, New Jersey 07920

Gene C. Schaerr
James P. Young
Sidley & Austin
1722 Eye Street, NW
Washington, DC 20006

M. Robert Sutherland
Richard M. Sbaratta
Bellsouth
1155 Peachtree Street, NE – Suite 1700
Atlanta, Georgia 30309-3610

Gary M. Epstein
Richard Cameron
Latham & Watkins
1001 Pennsylvania Avenue, NW
Washington, DC 20554

Alfred G. Richter, Jr.
Roger K. Toppins
Michael J. Zpevak
Charles J. Scharnberg
SBC Telecommunications, Inc.
One Bell Plaza – Room 3003
Dallas, Texas 75202

Jay C. Keithley
Leon M. Kestenbaum
Peter N. Sywenki
Richard Juhnke
Sprint Corporation
1850 M Street NW – 11th Floor
Washington, DC 20036

Edward Shakin
1320 North Court House Road – 8th Floor
Arlington, Virginia 22201

Cheryl A. Tritt
Frank W. Krogh
Christa M. Parker
Morrison & Foerster LLP
2000 Pennsylvania Avenue, NW
Washington, DC 20007

George Bochetto
Jeffrey W. Ogren
Bochetto & Lentz, P.C.
1524 Locust Street
Philadelphia, Pennsylvania 19102